

**BEFORE THE PUBLIC UTILITIES COMMISSION
OF THE STATE OF CALIFORNIA**



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Order Instituting Rulemaking on the
Commission's Own Motion into Combined Heat
and Power Pursuant to Assembly Bill 1613

Rulemaking 08-06-024
(Filed June 26, 2008)

**APPLICATION OF THE ALLIANCE FOR RETAIL ENERGY MARKETS
FOR REHEARING OF DECISION 09-12-042**

Daniel W. Douglass
Gregory S.G. Klatt
DOUGLASS & LIDDELL
21700 Oxnard Street, Suite 1030
Woodland Hills, California 91367
Telephone: (818) 961-3001
Facsimile: (818) 961-3004
Email: douglass@energyattorney.com
klatt@energyattorney.com

Attorneys for the
ALLIANCE FOR RETAIL ENERGY MARKETS

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TABLE OF CONTENTS

I.	INTRODUCTION	1
II.	THE DECISION’S ALLOCATION OF AB 1613 CONTRACT COSTS TO UNBUNDLED CUSTOMERS, WHO WILL NOT RECEIVE ANY TANGIBLE BENEFITS FROM THE CONTRACTS, IS UNLAWFUL	4
A.	Unbundled Customers Will Not Receive Any of the Real Benefits of AB 1613 Contracts.....	4
B.	Any Intangible Benefits That CHP Systems May Produce Are Not a Valid Basis Upon Which to Allocate AB 1613 Contract Costs.....	6
1.	The “intangible benefits” identified in the Decision are, at best, highly speculative.	7
2.	Non-Utility LSEs (and their customers) will bear their own GHG compliance costs.	8
3.	The Commission has abused its discretion in allocating AB 1613 contract costs on the basis of indirect societal benefits.	8
III.	CONCLUSION.....	11

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Pursuant to Rule 16.1 of the Commission's Rules of Practice and Procedure, the Alliance for Retail Energy Markets (AReM)¹ hereby submits this application for rehearing of Decision (D.) 09-12-042, *Decision Adopting Policies and Procedures for Purchase of Excess Electricity Under Assembly Bill 1613*, dated December 17, 2009 (hereinafter, "the Decision"). As the Decision was issued on December 21, 2009, this application for rehearing is timely filed.

I. INTRODUCTION

AReM seeks a limited rehearing of the Decision to rectify legal errors in the Commission's allocation of the costs and benefits of standard contracts for purchases of excess electricity from eligible combined heat and power (CHP) systems by investor owned utilities (IOUs) pursuant to Assembly Bill (AB) 1613 (Cal. Stats. 2007, ch. 713).

AB 1613, codified as Pub. Util. Code § 2840 et seq., established the Waste Heat and Carbon Emissions Reduction Act, which among other things imposes certain

¹ AReM is a California mutual benefit corporation formed by electric service providers that are active in California's direct access market. The positions taken in this filing represent the views of AReM but not necessarily the affiliates of its members with respect to the issues addressed herein.

responsibilities on the Commission relating to the purchase of excess electricity from eligible CHP systems by electrical corporations. In the Decision, the Commission adopted policies, procedures and the aforementioned standard contracts for such purchases by the state's three largest electric IOUs, Pacific Gas and Electric Company, Southern California Edison Company, and San Diego Gas & Electric Company. In addition, the Commission determined the allocation of the costs and benefits of AB 1613 contracts among ratepayers.

Under the Decision and the terms of the adopted AB 1613 contracts, the costs incurred by the buying utility will include the contract price for the power product, which will be based on the costs of a new combined cycle gas turbine, and may also include a 10% adder for CHP systems that are located in "high-value" load areas (i.e., a "location bonus").² In addition, the buying utility will be required to pay the greenhouse gas (GHG) compliance costs, if any, associated with the power product. The benefits conveyed to the buying utility under the standard contracts include all of the energy, capacity benefits and environmental attributes associated with the power product.³

Pub. Util. Code § 2841(e),⁴ enacted as part of AB 1613, provides that "[t]he costs and benefits associated with any tariff or contract entered into by an electrical corporation pursuant to this section shall be allocated to all benefiting customers." The obvious corollary of this statutory requirement is that AB 1613 contract costs may only be allocated to "benefiting customers" (i.e., customers of the buying utility that actually

² Decision, p. 38. (The page numbering of the version of the Decision posted on the Commission's website starts at page 2.)

³ Decision, pp. 49, 50-51 and 59.

⁴ Unless stated otherwise, all statutory references hereinafter are to the Public Utilities Code.

benefit from the contracts). A further corollary is that the Commission cannot allocate costs while withholding benefits.

In the Decision, the Commission determined that “[a]ll customers will receive the environmental and locational benefits produced by CHP systems participating under AB 1613.”⁵ The Commission concluded, therefore, that the costs of GHG compliance and location bonuses should be allocated to all retail customers (bundled and unbundled) of the buying utility.⁶

AReM submits that the Commission committed the following legal errors in allocating the costs and benefits of AB 1613 contracts:

- (1) Given that under the terms of the standard contracts all of the tangible benefits of the contracts are conveyed to the buying utility, and given that the Decision fails to provide for the allocation of any of those benefits to unbundled customers (i.e., direct access customers and community choice aggregation customers), allocating any of the costs of AB 1613 contracts to unbundled customers while failing to equally allocate the benefits violates § 2841(e) and is therefore unlawful.
- (2) Allocating the costs of GHG compliance and location bonuses to all customers based solely on indirect societal benefits that may be produced by CHP systems is inconsistent with Commission precedent and the principle of cost causation, arbitrary, and unfairly discriminatory, and is therefore an unlawful abuse of the Commission’s discretion.

⁵ Decision, Finding of Fact 13.

⁶ Decision, Conclusions of Law 1 and 4.

II. THE DECISION'S ALLOCATION OF AB 1613 CONTRACT COSTS TO UNBUNDLED CUSTOMERS, WHO WILL NOT RECEIVE ANY TANGIBLE BENEFITS FROM THE CONTRACTS, IS UNLAWFUL.

The Commission has committed a fundamental legal error in the Decision by authorizing the IOUs to allocate costs associated with their AB 1613 contracts to all of their customers (bundled and unbundled) when only the utilities and their bundled customers will receive the tangible contract benefits. The clear and unambiguous meaning of § 2841 is that the Commission is required to allocate the costs of such contracts to all customers who will benefit from the contracts. It follows that allocating any of the costs of AB 1613 contracts to customers who will not receive any real benefits from the contracts would violate § 2841 and is therefore unlawful.

A. Unbundled Customers Will Not Receive Any of the Real Benefits of AB 1613 Contracts.

In essence, the AB 1613 contracts are standard contracts for the purchase of excess electricity generated by CHP systems (i.e., electricity that is not consumed on site) that the IOUs are required by law to offer to eligible CHP systems. Under the express terms of the adopted AB 1613 contracts, all of the benefits of this power product, including energy, capacity benefits and associated environmental attributes, are conveyed to the buying utility.⁷ Therefore, as the following analysis shows, the only customers that will receive those benefits, which are the only tangible benefits of the contracts, are the buying utility's bundled customers.

⁷ Standard Contract Terms 3.01(a) (Power Product) and 3.02 (Resource Adequacy Rulings); see also Decision, p. 59 and Conclusion of Law 19.

First, and most obviously, the buying utility will receive all of the energy available under the contracts,⁸ which energy will then be consumed by the utility's bundled customers.

Second, the capacity value of the CHP systems under contract to a utility will be conveyed to the buying utility.⁹ The utility will then be able to count that capacity toward its resource adequacy (RA) requirements, including Local RA capacity associated with any CHP system located in congested areas receiving an extra "locational adder" in its contract payment.¹⁰ This RA capacity transfer allows the utility (and thus its bundled customers) to avoid the costs of procuring capacity that would otherwise have to be purchased from other resources to meet those requirements.

Third, any renewable energy credits (RECs) associated with the power product purchased under a contract will be conveyed to the buying utility.¹¹ The RECs can then be counted toward the utility's Renewable Portfolio Standard (RPS) requirements, thereby allowing the utility (and thus its bundled customers) to avoid the costs of procuring renewable energy or RECs that would otherwise need to be purchased from other sources to meet those requirements.

Fourth, the avoided GHG emissions associated with the power product will be attributed to the buying utility,¹² thereby allowing the utility (and thus its bundled customers) to avoid the costs of GHG emissions credits or non-compliance penalties that it might otherwise incur.

⁸ Standard Contract Term 3.01(a); see also Decision, p. 59.

⁹ Standard Contract term 3.02.

¹⁰ Decision, p. 24.

¹¹ Standard Contract Term 3.01(b) (Green Attributes) and Exhibit A (Definitions).

¹² Id.

Lastly, AReM notes that the Decision could have allocated a portion of the benefits of the AB 16 13 contracts (energy, capacity and environmental benefits to load serving entities (LSEs) that provide commodity service to unbundled customers. That would have been consistent with the “benefiting customers” approach followed in D.06-07-029, in which the IOUs were authorized to procure new generation capacity on behalf of all customers, all customers were allocated the capacity benefits, and the Cost Allocation Mechanism was established to allocate the costs of that capacity to all customers.

AReM is not advocating that the CAM approach be utilized for AB 1613 contracts; rather, AReM is contrasting the CAM approach and that following in the Decision, which makes no allocation of benefits to unbundled customers. As it stands, the Decision clearly errs in finding that unbundled customers are “benefiting customers” for purposes of § 2841(e) when they will not receive any of the benefits of the power products purchased under AB 1613 contracts (i.e., energy, capacity and environmental benefits).

B. Any Intangible Benefits That CHP Systems May Produce Are Not a Valid Basis Upon Which to Allocate AB 1613 Contract Costs.

The Decision identifies three “intangible” benefits produced by CHP systems—reduced GHG emissions, potential reduction in congestion, and more efficient utilization of natural gas—that it asserts all customers will receive.¹³ On that basis, the Decision finds that all IOU customers (bundled and unbundled) are “benefiting customers” for purposes of § 2841(e), and therefore all IOU customers should be

¹³ Decision, p. 22.

allocated the costs associated with those benefits.¹⁴ The Decision asserts further that this determination is supported by D.02-11-074, in which, according to the Decision, “the Commission determined that all retail end-use customers should bear cost responsibility [for the costs associated with power purchased by the Department of Water Resources (DWR) between January 17 and February 2, 2000] because these purchases had served to stabilize the entire electric grid during the Energy Crisis.”¹⁵ This line of reasoning has several fatal flaws.

1. The “intangible benefits” identified in the Decision are, at best, highly speculative.

First, the Decision’s finding that customers will receive some intangible benefits that may or may not be produced by CHP systems is, at best, highly speculative. In order for customers to actually benefit, a reduction in GHG emissions resulting from the operation of CHP systems must have a measurable effect on anthropogenic global warming, the location of CHP systems must have a measurable effect on congestion (i.e., reduced transmission costs or increased system reliability), and the more efficient utilization of natural gas must have a measurable effect on natural gas prices. Further, while the costs of the “locational adder” are charged to the unbundled customers, the Decision makes no attempt to allocate the only conceivable benefit of these costs to such customers, namely the associated Local RA capacity.

¹⁴ The specific costs that the Decision authorizes the IOUs to allocate to all customers are the GHG compliance costs and the so-called location bonuses for applicable AB 1613 contracts. (Decision, p. 25, Finding of Fact 23, and Ordering Paragraph 7.)

¹⁵ Decision, p. 23.

Tellingly, the Decision provides no analysis on these issues; instead, it simply makes a conclusory finding that CHP systems will produce such benefits and that all customers will receive those benefits. The Decision therefore violates § 1705, which requires Commission decisions to contain findings of fact and conclusions of law on all issues that are material to the Commission’s decision or order.¹⁶

2. Non-Utility LSEs (and their customers) will bear their own GHG compliance costs.

Second, non-utility LSEs that serve unbundled customers will bear the costs of their own GHG compliance (in the form of higher prices for electricity) the same as the IOUs, and those costs will necessarily be passed on to their customers. Since unbundled customers will already be paying the GHG compliance costs associated with the energy they consume, it would be unreasonable and unfairly discriminatory to require them to subsidize the GHG compliance costs associated with the energy that bundled customers consume. The Decision therefore violates the just and reasonable requirement of § 451 and the prohibition on unreasonable and unfairly discriminatory rates contained in § 453.

3. The Commission has abused its discretion in allocating AB 1613 contract costs on the basis of indirect societal benefits.

The Decision states that basing the allocation of the costs of the so-called “environmental and locational benefits” produced by CHP systems is supported by prior Commission decisions, citing D.02-11-074. However, the Decision’s reliance on D.02-11-074 is clearly misplaced. In the portion of D.02-11-074 cited in the Decision, the Commission determined the policy for allocating the costs associated with power

¹⁶ See also § 1757.1(a)(4).

purchased by DWR between January 17 and February 2, 2000. The Commission determined that those costs, which were to be collected through the DWR Bond Charge, should be “spread over all customer usage,” with certain exceptions not relevant here.¹⁷ The Commission based this policy determination in part on the fact that all customers benefited from the stabilization of the grid resulting from DWR’s purchases. Importantly, however, the Commission expressly stated that it was not following “the principle of cost causation” to allocate the bond-related costs.¹⁸

Even more importantly, the Commission had already determined in a prior decision that direct access customers that had not consumed DWR-procured power during the period in question should not be required to pay any DWR bond costs. The issue of the cost responsibility of direct access customers for DWR bond costs was determined in D.02-11-022, which was issued two weeks prior to D.02-11-074. In that decision, the Commission excluded direct access customers who were continuously served by electric service providers (ESPs) during the energy crisis (referred to as “Continuous DA Customers”) from the Direct Access Cost Responsibility Surcharge (DA CRS), including the DWR Bond Charge.¹⁹ This was explicitly done because such customers did not consume DWR-procured power during the energy crisis and therefore did not benefit from DWR’s power procurement.²⁰ The Commission explained its decision as follows:

¹⁷ D.02-11-074, Attachment A, at 25.

¹⁸ Id.

¹⁹ D.02-01-011, Conclusion of Law 14 and Ordering Paragraph 4.

²⁰ Id., Conclusion of Law 15.

Attempting to assign a charge to DA customers based solely on indirect societal benefits would be arbitrary and speculative. Moreover, it would be unfairly discriminatory to assess a uniform bond charge among DA customers when some of them had actually consumed DWR-procured power while others had consumed none.²¹

This explanation has a direct bearing on the faulty logic employed by the Decision. Contrary to the assertion made in the Decision that the Commission allocated the DWR bond costs to “all customers” in D.02-11-074 on the grounds that all customers benefited from the stabilization of the grid, the Commission actually allocated the DWR bond costs to all customers that had consumed DWR-procured power. Moreover, the Commission’s determination that all future customers should also pay the DWR Bond Charge despite their never having consumed DWR-procured power was an explicit departure from the principle of cost causation, a departure that the Commission found appropriate in the limited case of DWR bond costs for the following reasons:

- The long period over which the bond charges will be collected breaks the linkage between those for whom the power was purchased and those responsible for repayment.
- Use of the principle of “cost causation” to allocate bond-related costs was unwarranted given that the prices DWR paid for power during the subject period, which was a declared state of emergency, had little relationship to the cost of producing that power.
- The bond costs were not routine costs arising from utility operations.²²

In contrast to the DWR bond costs, there is a clear link between the costs of AB 1613 contracts and the IOUs’ bundled customers. That linkage is the power products purchased under the contracts, the tangible benefits of which will flow directly,

²¹ D.02-11-022, p. 61.

²² D.02-11-074, pp. 25-26 and Finding of Facts 17, 20,

and solely, to bundled customers under the Decision. The costs of the AB 1613 contracts are directly related to the benefits of the power product. And the IOUs' purchases of power under AB 1613 contracts will be part of the IOUs' routine procurement operations. Accordingly, there is no valid reason for the Commission to depart from their customary principle of cost causation in allocating the costs of the AB 1613 contracts. Moreover, allocating contact costs based on indirect societal benefits such as the highly speculative "intangible benefits" identified in the Decision is inconsistent with the Commission's prior decisions, arbitrary, unfairly discriminatory, and an abuse of the Commission's discretion.²³

III. CONCLUSION

For the above reasons, the Commission should grant a rehearing of D.09-12-042 to rectify the legal errors in the allocation of the costs and benefits of AB 1613 contracts adopted therein.

Respectfully submitted,



Gregory S.G. Klatt
DOUGLASS & LIDDELL
21700 Oxnard Street, Suite 1030
Woodland Hills, California 91367
Telephone: (818) 961-3001
Facsimile: (818) 961-3004
Email: douglass@energyattorney.com
klatt@energyattorney.com

Attorneys for the
ALLIANCE FOR RETAIL ENERGY MARKETS

January 20, 2010

²³ See discussion of D.02-11-022 and D.06-07-029 above.

CERTIFICATE OF SERVICE

I hereby certify that I have this day served a copy of *Application of the Alliance for Retail Energy Markets for Rehearing of Decision 09-12-042* on all parties of record in proceeding *R.08-06-024* by serving an electronic copy on their email addresses of record and by mailing a properly addressed copy by first-class mail with postage prepaid to each party for whom an email address is not available.

Executed on January 20, 2010, at Woodland Hills, California.



Michelle Dangott

SERVICE LIST – R.08-06-024

abb@eslawfirm.com
akbar.jazayeri@sce.com
alho@pge.com
amber.wyatt@sce.com
atrowbridge@daycartermurphy.com
ayk@cpuc.ca.gov
bcragg@goodinmacbride.com
beth@beth411.com
bjl-lec@sbcglobal.net
blair@cipa.org
blaising@braunlegal.com
bmcc@mccarthy.com
bobgex@dwt.com
brbarkovich@earthlink.net
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californiadockets@pacificcorp.com
carol.schmidfrazee@sce.com
Case.Admin@sce.com
cem@newsdata.com
chilen@NVEnergy.com
cjm@cpuc.ca.gov
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css@cpuc.ca.gov
dakinports@semprautilities.com
dansvec@hdo.net
dbp@cpuc.ca.gov
dcarroll@downeybrand.com
demorse@omsoft.com
dennis@ddecuir.com
dgrandy@caonsitegen.com
dniehaus@semprautilities.com

douglass@energyattorney.com
dws@r-c-s-inc.com
egrizard@deweysquare.com
ek@a-klaw.com
eks@cpuc.ca.gov
ell5@pge.com
epoole@adplaw.com
filings@a-klaw.com
gcollord@arb.ca.gov
glemei@energy.state.ca.us
HYao@SempraUtilities.com
hym@cpuc.ca.gov
jbarnes@summitblue.com
Jcox@fce.com
jims@vea.coop
jig@eslawfirm.com
jody_london_consulting@earthlink.net
jon.bonk-vasko@energycenter.org
jordan.white@pacificcorp.com
joyw@mid.org
jrathke@capstoneturbine.com
jwwd@pge.com
kar@cpuc.ca.gov
karen@kclindh.com
klatt@energyattorney.com
kroderic@arb.ca.gov
laura.genao@sce.com
liddell@energyattorney.com
lkelly@energy.state.ca.us
lmh@eslawfirm.com
lschavrien@semprautilities.com
marcel@turn.org
marci.burgdorf@sce.com
mbe@cpuc.ca.gov

mc3@cpuc.ca.gov
mflorio@turn.org
mgarcia@arb.ca.gov
mike.montoya@sce.com
mpa@a-klaw.com
mramirez@sflower.org
mrw@mrwassoc.com
MWZ1@pge.com
nes@a-klaw.com
norm@pzallc.com
ralf1241a@cs.com
regrelcpuccases@pge.com
rkmoore@gswater.com
rmm@cpuc.ca.gov
rnevis@daycartermurphy.com
rogerv@mid.org
sberlin@mccarthy.com
Sean.Beatty@mirant.com
sendo@ci.pasadena.ca.us
sephra.ninow@energycenter.org
sha@cpuc.ca.gov
skg@cpuc.ca.gov
sls@a-klaw.com
spatrick@sempra.com
srovetti@sflower.org
sue.mara@rtoadvisors.com
taj8@pge.com
tburke@sflower.org
tcr@cpuc.ca.gov
thomas.r.del.monte@gmail.com
tomb@crossborderenergy.com
tzentai@summitblue.com
wamer@kirkwood.com
wbooth@booth-law.com